pretenses the surety assumes a contingent obligation or when, on the default of the principal debtor, the obligation becomes absolute, or only when the surety actually parts with the *res* (money)? In most cases, as in the principal one, the *res* actually passes before the discharge of the bankrupt and there is no doubt that "property" is obtained, but where all that is obtained is a promise to pay money if the principal debtor fails to pay, and at the time of the discharge in bankruptcy of the latter the surety has not parted with a *res,* but his obligation to do so has become absolute, it can at least be said, applying the rules laid down in the previous paragraph as to obtaining "property" by false pretenses and substituting the phrase "obligation to part with property" for the words "property" and *res,* that the obligation is obtained by false pretenses. Under the early statutes such phrases as "goods, wares, and merchandise" and "money or property" were not broad enough to include promissory notes and the like, and would not include this obligation. The operation of modern statutes has been extended by adding such words as "money, goods, chattels, things in action, and evidences of debt." *People* v. *Reed,* 70 Cal. 533; *State of Iowa* v. *Patty,* 97 Ia. 373. There is not such a difference in the nature, purpose, and language of the BANKRUPTCY ACT and of the section under discussion as to warrant a distinction, hence an additional requirement must therefore be added to the definition laid down in the previous paragraph, namely, that the *res* must actually be parted with by the person to whom the false pretenses are made. If the absolute obligation to pay is not "property," neither is the contingent or inchoate obligation.

It will be interesting to note the result if this precise problem is ever brought before a court, if it should be held that the *res* must actually pass and if the decision in *Williams, et al* v. *United States Fidelity and Guaranty Company,* 236 U. S. 549, 35 Sup. Ct. 289, in which no question of false pretenses is involved, is followed. In that case the principal had defaulted and had received a discharge in bankruptcy from his obligation to the principal, but the surety had not at that time paid the principal creditor. It was nevertheless held that the principal debtor's inchoate obligation to indemnify his surety was also discharged. But if the surety's inchoate obligation or even his absolute obligation, obtained by false pretenses, is not "property" within the meaning of § 17, and if the *Williams* case is followed, the surety, after the principal's discharge, will have no redress against him and will still be liable to the principal creditor. For a full discussion of *Williams et al.* v. *United States Fidelity and Guaranty Company* see 13 MICH. L. REV. 500.

S. D. F.

SET-OFFS AND PREFERENCES.—§ 68a of the BANKRUPTCY ACT provides that "in all cases of mutual debts or mutual credits between the estate of a bankrupt and a creditor the account shall be stated and one debt shall be set off against the other, and the balance only shall be allowed or paid." The courts are experiencing considerable difficulty in determining whether this provision makes it possible for a bank to retain as against the trustee in bankruptcy the amount of a depositor's check received by the bank within four months of the depositor's insolvency, and with reasonable cause to be-

lieve that he was insolvent, in satisfaction to that amount of a matured obligation due the bank from the depositor. Obviously, one of the incidental questions involved in the determination of this problem is whether the receipt of a check prevents the transaction from being denominated a "set-off." In a case decided in 1872 under the BANKRUPTCY ACT of 1867 (the provisions of which in reference to set-offs and preferences are identical with the existing act so far as the present discussion is concerned) the Supreme Court of the United States answered this question in the affirmative. *Traders' National Bank* v. *Campbell,* 14 Wall. (81 U. S.) 87. The court was of the opinion that the receipt of the check shows that the bank treats the deposit as the property of the depositor and is not relying upon its right of set-off. It was therefore held that the giving of the check constituted a payment which the assignee in bankruptcy was allowed to recover as a voidable preference; and the court intimates that if the bank had simply charged the depositor's account, the transaction would have amounted to a set-off. But this holding does not seem to have found favor with the inferior courts at that time. Two years later, a federal district court held that the receipt by the bank of the depositor's check constituted a set-off. On appeal to the circuit court, the state of the record was such that the question was not then open to review, but the circuit court ventured the dictum that the giving of the check did not prevent the transaction from being a set-off "unless the opinion of the Supreme Court in the case of *Traders' National Bank* v. *Campbell* decides differently * * * Whether the case cited holds otherwise it is not necessary nor indeed proper to inquire." *Blair* v. *Allen,* Fed. Cas. No. 1,483. In 1879, another circuit court reached a decision opposed to the views expressed by the Supreme Court. *Robinson* v. *Wisconsin M. & F. Ins. Co. Bank,* Fed. Cas. No. 11,969. In the course of its opinion the court says: "Upon the argument, the form of the transaction was dwelt upon, namely that a check was drawn and given for the amount of the note, and that the parties spoke of it in the course of their interview, as a payment. But we are not to sacrifice substance to form, but rather to go beyond the mere form and see what the substance and effect of the transaction was. And doing so, we find that it was in fact an adjustment of mutual debts." In reference to the *Traders' Bank* case, the following statement is made: "Taking the whole case together there was evidently a flagrant attempt on the part of the bank to obtain fraudulent preferences, and the several transactions between it and the bankrupts, which gave rise to the subsequent controversy, were so intermingled that the court seems to have found it necessary to condemn the whole as amounting to a fraudulent and unlawful proceeding." Since the *Traders' Bank* case appears to be the only express adjudication by the United States Supreme Court on the question involved it may not be amiss to notice those of its facts which are peculiar. The debtors of the bank in that case gave to the bank their demand note for the whole amount of their debt, with a power to confess judgment. On the next day the bank credited the note to the extent of the debtor's deposit and entered a judgment for the balance. The note was so credited because of the receipt of the debtor's check for the amount of the

deposit. After judgment, execution issued and a stock of goods belonging to the debtors was levied upon. In less than one month a petition in bankruptcy was filed against the debtors and they were adjudicated bankrupt. Later the debtor's stock of goods was sold under the execution of the bank and also a certain sum which the bank had received before bankruptcy by way of collections of drafts for the debtors. The amount received from the sale of the stock of goods was obviously a preference. But it is submitted that the court, had it been so disposed, could very easily have allowed a recovery either for this amount or for this amount plus the amount of the collections without having found it necessary to "condemn the whole." And if we are to determine the reason for the court's allowing the assignee to recover he amount of the check, it is therefore only fair to the court and in accord with the dictates of common sense, that we accept the reason the court has stated. It may be noted in passing that the amount of the collections was allowed to be recovered because, according to the court's statement, the bank in causing the sheriff to levy upon the fund collected, treated it as the property of the debtors and did not rely upon its "own right of set-off." Both of the two last-mentioned amounts were therefore recovered because of the same general reason

The *Traders' Bank* case stands practically alone among the cases decided under the BANKRUPTCY ACT of 1867. Before the decision of the *Traders' Bank* case, it was held in 1869 in *Hough* v. *First National Bank*, Fed. Cas. 6,721, that the giving of the check is in substance an adjustment of mutual debts and not a payment. In 1871, in *In re Warner et al.*, Fed. Cas. 17,177, it was thought that the giving of the check could constitute such fraudulent preference as to prevent the discharge of the bankrupt. But whatever importance might be accorded this holding, is seriously impaired by the fact that the court, in the course of its opinion, seems to be utterly oblivious of the set-off provision of the statute, and also seems to deny the general right to set-off mutual accounts independent of the BANKRUPTCY ACT.

The first intimation since the enactment of the present bankruptcy law as to whether the rule of the *Traders' Bank* case is to be followed, occurred in the course of the opinion of the United States Supreme Court in *New York County National Bank* v. *Massey*, 192 U. S. 138, 146. The court, in upholding the generally-accepted proposition that a set-off should be allowed between a bank and a bankrupt depositor, refers to the *Traders' Bank* case as not being an authority to the contrary because "the right of set-off was not relied upon, but a deposit was seized upon a judgment which was a preference." The court here, of course, fails to notice that a check drawn upon the deposit was given to the bank and that the execution was levied upon the amount the bank had received from collecting the bankrupt's drafts. But nevertheless the intimation is strong that the court in 1903 believed that the levying of an execution upon a deposit cannot constitute a set-off, although the transaction results in nothing more than the settlement of mutual debts; because the bank in so doing is treating the deposit as the property of the depositor. But as already noted in the *Traders' Bank* case, this reasoning applies equally as well to the transaction in which the bank receives a check

from the depositor drawn upon the deposit. This meager reference to its former decision therefore raised a strong presumption that the Supreme Court would still adhere to the doctrine of the *Traders' Bank* case.

But since *Studley* v. *Boylston National Bank,* 229 U. S. 523, the presumption lies very much in the opposite direction. In this case, the bank received the depositor's check without reasonable cause to believe that the depositor was insolvent. Therefore, even if the giving of the check constituted a preference, it did not here constitute a voidable preference. The court was not called upon to decide any question of set-off; and the following statement of the court, so far as the checks were concerned, might have disposed of the whole case: "But if * * * the bank had no reasonable cause to believe such transfers would effect a preference the payments by checks for $15,000 are as much protected as if on the same dates similar checks had been given in payment of like amounts due another bank with which the Collver Co. [the bankrupt] kept no account." The court, however, undertakes also to consider the case from the viewpoint of the question of set-off, and comes to the conclusion that whether a bank charges the depositor's account or whether the depositor gives the bank a check is immaterial; for in either event the transaction amounts to no more than a book entry "equivalent to the voluntary exercise by the parties of the right of set-off." *Dicta* to the same effect occur in the following cases based on similar facts: *Putnam* v. *U. S. Trust Co.,* 223 Mass. 199, 111 N. E. 969; *Walsh* v. *First National Bank,* 201 Fed. 522, 120 C. C. A. 30. Such a transaction was recognized as a set-off, by way of *obiter* also in *Chisholm* v. *First National Bank,* 269 Ill. 110 (see 14 MICH. L. REV. 147, 149), and by way of express adjudication in *Toof* v. *City National Bank,* 206 Fed. 250, 124 C. C. A. 118, and in *American Bank & Trust Co.* v. *Coppard,* 227 Fed. 597, 142 C. C. A. 229. Holdings to the contrary, however, may be found in *In re Scheizer,* 130 Fed. 631; *Ridge Ave. Bank* v. *Studheim,* 145 Fed. 798, 76 C. C. A. 362; *In re Starkweather & Albert,* 206 Fed. 797; *In re National Lumber Co.,* 212 Fed. 928, 129 C. C. A. 448; *Knoll* v. *Commercial Trust Co.,* 229 Pa. St. 197.

Those courts which refuse to treat the transaction in question as a set-off are probably influenced by a desire to construe § 68a strictly, since this section is inconsistent with one of the two main general purposes of the BANKRUPTCY ACT, viz.: the according of equal treatment to creditors. But after all, the distinction which these courts make is, as the early *Robinson* case points out, a distinction in form and not in substance. If the bank has the right to charge the depositor's account without his consent the bank should not be made to suffer merely because, by means of a check, it has received the depositor's consent. And general judicial recognition of this distinction would have no other effect than to cause banks always to charge the account without positive action on the part of the depositor, with the result that the general creditors will have been in no way benefited by the distinction.

It would seem that the transaction under consideration might be more vitally attacked by making a distinction between a set-off before bankruptcy

and a set-off after bankruptcy; since § 68a provides only for a set-off after bankruptcy. Yet all the cases cited *supra* which hold that the transaction amounts to a set-off also hold that it matters not that the set-off occurred within the four months before bankruptcy (except *Toof* v. *City National Bank,* in which case the check was given after the petition was filed). The *Studley* case also contains *dicta* to this effect. This view is further supported by an apparently unanimous line of authorities which allow a bank to charge the bona fide depositor's account within the four months' period when no check is given, although the bank had reasonable cause to believe the depositor was insolvent. Among the modern cases so holding may be cited: *Continental & Commercial Trust & Savings Co.* v. *Chicago Title & Trust Co.,* 229 U. S. 435; *Lowell* v. *International Trust Co.,* 158 Fed. 781, 86 C. C. A. 137; *Germania Savings Bank & Trust Co.* v. *Loeb,* 188 Fed. 285, 110 C. C. A. 263; *West* v. *Bank of Lakhoma,* 16 Okla. 328; *Habeggar* v. *First National Bank,* 94 Minn. 445; *Chisholm* v. *First National Bank,* supra; *Booth* v. *Prete,* 81 Conn. 636.

But to sustain the proposition that no set-off within the four-month period is protected by § 68, certain intimations will be found in the cases of *Ridge Ave. Bank* v. *Studheim* and in *In re National Lumber Co.* which have already been cited to the proposition that a transaction in which a check is given is not a set-off. And in the cases of *Putnam* v. *United States Trust Co.* and *Walsh* v. *First National Bank,* referred to above as containing *dicta* in favor of the proposition that the giving of a check does not prevent the transaction from being a set-off, will be found statements to the effect that if the check is received within the four months, it is to be treated as a preference and its amount recovered if the bank has reasonable cause to believe that the depositor was insolvent. The *Putnam* case in fact actually allowed upon this theory the recovery of the amount of certain checks. This decision is of particular importance in showing that the dictum of the United States Supreme Court in the *Studley* case and the court's actual holding—without consideration of the question—in the case of *Continental & Commercial Trust & Savings Co.* v. *Chicago Title & Trust Co.* have not settled the controversy.

The *Studley* case in its dictum expresses the reason for allowing a set-off in the four-month period, as follows: "There is nothing in § 68a which prevents the parties from voluntarily doing before the petition is filed what the law itself requires to be done after proceedings in bankruptcy are instituted." In *Booth* v. *Prete,* supra, the court states: "The fact that the set-off in the present case was made by the bank prior to the filing of the bankruptcy petition does not affect the question because it did only what the law would have done had the bank waited until the petition was filed." Thus the same reason is generally alluded to. But it is respectfully submitted that the effect of the set-off before bankruptcy does not necessarily produce the same effect as would a set-off after bankruptcy. If no set-off occurs before bankruptcy, the depositor might, so far as § 68a is concerned, draw on the deposit which would otherwise be set off; and the result of his so doing, would be that after bankruptcy, the bank would receive less and

the general creditors would probably receive more than had a set-off occurred before bankruptcy. It is also worthy of notice in this connection that the decision of the United States Supreme Court that the deposit in the *Massey* case supra was not a preference is based upon the fact that the depositor retained the right to draw out the money at any time before his bankruptcy. Further authority of some value contrary to the *Studley* dictum may be found in those cases which allow the recovery of the amount of the deposit that has been appropriated to the discharge of an unmatured obligation before bankruptcy with reasonable knowledge to believe that the depositor is insolvent, although such a set-off is legal after bankruptcy. *Heyman* v. *Third National Bank,* 216 Fed. 685; *Shale* v. *The Farmers Bank,* 82 Kans. 649; *Irish* v. *Citizens Trust Co.,* 163 Fed. 880. But it must be admitted that the recent *Putnam* case, which holds that a set-off before bankruptcy constitutes a preference, oddly enough upon the authority of the *Studley* dictum, accepts the view that an unmatured obligation is subject to set-off within the four-month period; but nevertheless, as already mentioned, the court in this case treats a set-off before bankruptcy as a payment, and allows recovery in accordance with § 60 if the bank, at the time of the set-off occurred, had reasonable cause to believe that the depositor was insolvent.

Though there is nothing in § 68a which justifies a setting off of mutual debts in the four-month period before bankruptcy, it does not necessarily follow that the many courts which accept this view, arrive at an erroneous result. As the *Studley* case states, there is nothing in this section which prevents such a transaction before bankruptcy. Before the enactment of the BANKRUPTCY ACT, the bank had the right to make a set-off at least whenever the depositor's obligation had matured. Therefore, if this right is affected by the ACT, it must be by virtue of some provision other than that contained in § 68a. And where are we to find such provision? § 60, of course, suggests itself immediately with its provision in regard to preferences. But one essential element for the recovery of preference according to § 60 is that the "bankrupt shall have made a transfer." A similar element is essential for recovery under § 67e. Although the courts wisely incline to construe these sections liberally, it would seem very difficult to bring within their terms a transaction in which the bank charges the account of a bankrupt depositor who remains passive or even objects. And perhaps, as before suggested in another connection, the fact that the depositor has consented should make no difference. At first thought, it does not seem plausible that the framers of the BANKRUPTCY ACT meant to allow creditor banks greater privileges than have other creditors within the four months preceding the debtor's bankruptcy. But it is plain that the framers meant to allow them greater privileges after bankruptcy. This is indicative of a general policy. And furthermore, the statements made in the *Studley* and other cases to the effect that to deny the right of set-off within the four-month period would "so interfere with the course of business as to produce evils of serious and far-reaching consequence," are worthy of consideration as tending to show that the failure of Congress to provide language that would declare such a set-off invalid, was not inadvertent. M. W.